Office-Supreme Court, U.S.
FILED
DEC 22 1983
ALEXANDER L. STEVAS,
CLERK

No. 83-877

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

CURTIS H. JOHNSON and GLORIA JEAN JOHNSON, d/b/a OAK FARM LIVESTOCK and OAK FARMS, INC. and OAK FARMS SERVICE CO.,

Petitioners,

vs.

FIRST NATIONAL BANK OF MONTEVIDEO, MINNESOTA,

Respondent.

BRIEF OF RESPONDENT, THE FIRST NATIONAL BANK IN MONTEVIDEO, IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

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224-7233 — Banner Publishing Co., 227 E. 6th St., St. Paul, Minn. 55101 — 224-2323

QUESTION PRESENTED FOR REVIEW

In the absence of express authority under either state or federal law, does the Bankruptcy Court have the general equitable power to suspend indefinitely the running of Minnesota's statutory period of redemption following foreclosure?

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OPINIONS BELOW

The order of the Bankruptcy Court is unreported and is found on pages A-53 through A-56 of the Petition. The United States District Court opinion is reported at 19 Bankruptcy Reporter 650 (1983) and is reprinted on pages A-41 through A-52 of the Petition. The opinion of the Court of Appeals for the Eighth Circuit is reported at 719 F.2d 270 and is reprinted on pages A-3 through A-40 of the Petition.

JURISDICTION

The jurisdiction of this Court is based on 28 U.S.C. § 1254 (1) (1976) to review a judgment of the United States Court of Appeals for the Eighth Circuit entered on October 11, 1983.

CONSTITUTIONAL AND STATUTORY PROVISIONS

The Bankruptcy Court's order was entered under authority of Section 105(a) of the Bankruptcy Code of 1978:

> "The bankruptcy court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title."

11 U.S.C. § 105(a) (1982).

The Eighth Circuit's opinion also considered the application to this case of Sections 108 and 362 of the Bankruptcy Code of 1978. These sections are codified at 11 U.S.C. §§ 108 and 362 (1982) and are reprinted on pages ix through xiii of the Petition.

No constitutional issues have been raised in this case.

STATEMENT OF THE CASE AND STATEMENT OF FACTS

This case arises out of foreclosure proceedings commenced by respondent in September of 1980 against two Minnesota mortgages executed by petitioners in March, 1978 and May, 1979.[1]

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[1] The petitioners are a married couple and two corporations controlled by the couple. The petitioners have been treated throughout these proceedings as a single entity.

As contemplated by Chapter 580 of the Minnesota Statutes, the mortgaged property was sold at public auction on October 31, 1980. Respondent purchased the property at foreclosure for an amount equal to the entire unpaid balance of the secured indebtedness, together with the fees and expenses of sale allowed by statute.

Minnesota law granted the petitioners, or their assignee, a twelve month period within which to redeem the property from the foreclosure sale upon payment to respondent of the amount bid at sale, together with statutory interest from the date of sale. *See*, Minn. Stat. § 580.23 (1982). As is also contemplated by Minnesota law, petitioners remained in possession of the property during the redemption period. Respondent received no compensation for the use of the property by petitioners during the redemption period.

As discussed below, absent fraud or misconduct in connection with the foreclosure sale, Minnesota law does not permit an extension of the statutory period of redemption following foreclosure.

Petitioners did not exercise their statutory right to redeem. Instead, on October 8, 1981—eleven months and eight days after the foreclosure sale—petitioners filed a joint petition for reorganization under Chapter 11 under the Bankruptcy Code of 1978, at which time petitioners also commenced the instant action.

On October 20, 1981, the Honorable John J. Connelly, Judge of Bankruptcy Court, issued an order in which he found that "an exigency exists, and that the debtors have substantial equity" in the property purchased by respondent at foreclosure. Petition at A-55. Based on this finding, Judge Connelly "enjoined" the respondent "from further action to foreclose the property" described in its mortgage. *Id.* Expiration

of petitioners' time to redeem from the foreclosure sale was also extended "until further order of [the] Court." *Id.*

The Bankruptcy Court's order was affirmed by the District Court on March 13, 1982.

The decisions of the Bankruptcy and District Courts were not based on a specific provision of either state or federal law. Both decisions were instead based on the jurisdiction of the Bankruptcy Court under Section 105(a) of the Bankruptcy Code to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." 11 U.S.C. § 105(a) (1982).

On October 11, 1983 the Eighth Circuit reversed the District Court order, and petitioners now seek review by this Court.

REASONS FOR NOT GRANTING THE WRIT

1. The Eighth Circuit's Opinion Is Consistent With Prior Decisions Of This Court.

The Petition, perhaps in anticipation of this response, argues that the Eighth Circuit's opinion is inconsistent with this Court's decision in *Butner v. United States*, 440 U.S. 48 (1979) [hereafter "Butner"]. It is clear, on the contrary, that the Eighth Circuit's opinion is consistent both with *Butner* and with the long line of cases of which *Butner* is a part.

Butner involved a dispute as to whether a mortgagee's rights to rent generated during the pendency of a bankruptcy proceeding should be "determined by a federal rule of equity or by the law of the State where the property is located." *Id.* at 49. The Court, in rejecting application of a federal rule

of equity, emphasized the importance of state property laws in determining the relationship of the parties to a bankruptcy proceeding:

> Property interests are created and defined by state law . . . . [T]he federal bankruptcy court should take whatever steps are necessary to ensure that the mortgagee is afforded in federal bankruptcy court the same protection he would have under state law if no bankruptcy had ensued. This is the majority view, which we adopt today.

Id. at 55 and 56.

The Bankruptcy Court order in this case ignored the fundamental rule in Minnesota that the right of redemption is "dependent upon, and in all respects governed by the statute." *State ex rel. Anderson v. Kerr*, 51 Minn. 417, 53 N.W. 719 (1892). The Minnesota statute does not provide for an extension of the redemption period, and unless a "fraud has been practiced, no court can interpose conditions or qualifications in violation of the statute." *Id. See also, W. E. Suhring Co. v. Stafford*, 166 Minn. 430, 208 N.W. 136 (1926); *Hoover v. Johnson*, 47 Minn. 434, 50 N.W. 475 (1891). The Eighth Circuit recognized that the Bankruptcy Court, by substituting a federal rule of equity for Minnesota's property law, violated "the essential point . . . that in a properly administered scheme . . . the basic federal rule is that state law governs." *Butner*, 440 U.S. at 57.

It is true, of course, that the opinion in *Butner* also recognized the ability of the Bankruptcy Court to "deal with particular, individualized problems." *Butner*, 440 U.S. at 56. There is, however, nothing unique or individualized about the facts presented to the Bankruptcy Court in this case. The Bankruptcy Court's order in this case, on the contrary,

was based solely on a desire to preserve the petitioners' equity in the property purchased by the respondent at foreclosure. "It is precisely this concern, however, which the Minnesota legislature addressed by providing for a one-year period of redemption." *Johnson v. First National Bank of Montevideo*, 719 F.2d 270, 274 (8th Cir. 1983) [hereafter "Johnson"]. *See also, Tomasko v. Cotton*, 200 Minn. 69, 273 N.W. 628 (1937).

Petitioners would create an exception to the general rule of *Butner* to permit the Bankruptcy Court to disregard state property rights whenever a federal rule of equity might be more beneficial to the debtor or his trustee. The Eighth Circuit recognized that this interpretation of this Court's language, if adopted, would effectively overrule the holding reached in *Butner*.

Moreover, *Butner* cannot be isolated from the unbroken line of cases of which it is a part. This Court has consistently taken the position that the nature and the extent of a debtor's interest in property are to be determined by state law, and that "state laws are . . . suspended only to the extent of actual conflict with the system provided by the Bankruptcy Act of Congress." *Stellwagen v. Clum*, 245 U.S. 605, 613 (1918). *See also, Thompson v. Fairbanks*, 196 U.S. 516, 522 (1905); *Humphrey v. Tatman*, 198 U.S. 91, 93-95 (1905); *York Manufacturing Co. v. Cassell*, 201 U.S. 344, 352 (1906); *Thompson v. Magnolia Petroleum Co.*, 309 U.S. 478, 483-484 (1940); *Lewis v. Manufacturers National Bank*, 364 U.S. 603 (1961).

The petitioners have requested that this Court abandon the traditional deference accorded to state law under the federal bankruptcy act. For the reasons indicated below, the respondent believes that this is an inappropriate case in which to

embark on such a fundamental reexamination of this Court's historic interpretation of federal bankruptcy law.[2]

2. Because Of The Wide Variation Among The State Statutes Governing Mortgage Foreclosures, The Eighth Circuit's Opinion Is Likely To Have Little Impact Outside The State Of Minnesota.

Minnesota law provides for issuance of a sheriff's certificate of sale at the time of the foreclosure sale. Minn. Stat. § 580.12 (1982). This certificate must be recorded within twenty days of the sale, and "when so recorded, upon expiration of the time for redemption, shall operate as a conveyance to the purchaser or his assignee of all the right, title, and interest of the mortgagor" in the property described in the certificate "without any other conveyance." *Id.*

The statutory period of redemption in Minnesota may extend for either six or twelve months.[3] The mortgagor is

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[2] The Petition also argues that the Eighth Circuit's opinion is inconsistent with the Court's opinion in *United States v. Whiting Pools, Inc.*, —— U.S. ——, 103 S. Ct. 2309 (1983), a case dealing with the relationship between the "turn-over" provisions of Section 543 of the Bankruptcy Code and the levy and distraint provisions of the Internal Revenue Code. *Whiting Pools*, however, did not consider the extent to which the Bankruptcy Court may act in areas not specifically addressed in the Bankruptcy Code, and the Court's opinion in the case is therefore of little relevance to the issues addressed by the Eighth Circuit.

[3] A twelve month period of redemption is required if:

a. The mortgage was executed prior to July 1, 1967, or

b. The mortgagor had paid more than one-third of the principal balance of the mortgage, or

c. As is the case here, the mortgage covered more than ten acres of property.

Minn. Stat. § 580.23(2) (1982).

generally entitled to remain in possession of the property during the entire period of redemption.[4] As noted above, however, absent fraud or misconduct in connection with the sale, the redemption period may not be extended beyond the statutory period, and title to the mortgaged property passes automatically to the purchaser at foreclosure after the period of redemption. In Minnesota, lapse of time alone vests a purchaser at foreclosure with full title. *In re Klein*, 9 F. Supp. 57 (D. Minn. 1934).

The Eighth Circuit held, in the context of Minnesota's specific statutory scheme, that the Bankruptcy Code does not contain a provision which may operate to indefinitely extend expiration of Minnesota's period of redemption. Accordingly, the Eighth Circuit held that the authority given to the Bankruptcy Court under Section 105 of the Bankruptcy Code to "carry out the provisions of this title" does not permit entry of an order suspending indefinitely the running of this statutory time period.

The Petition refers to a number of other jurisdictions which provide for the automatic passage of title to a purchaser at foreclosure. The Petition suggests that the Eighth Circuit's opinion may be directly relevant to cases arising in these other jurisdictions. The Petition, however, ignores the endless variation among state foreclosure statutes. These differences in state law, it is clear, will severely limit the impact of the Eighth Circuit's opinion.

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[4] The exceptions to the general rule arise in cases involving waste of the property, *see, e.g., Cross Companies, Inc. v. Citizens Mortgage Investment Trust*, 305 Minn. 111, 232 N.W.2d 114 (1975), and in certain limited situations involving assignments of rent given in connection with mortgage loans in excess of $500,000. *See*, Minn. Stat. §§ 559.17(2) and 576.01(2) (1982).

State foreclosure statutes typically contemplate that the mortgaged property will be offered for sale at an auction conducted by either a public official or by the lienholder. *See generally*, Committee on Mortgage Law and Practice, *Cost and Time Factors in Foreclosure of Mortgages*, 3 Real Prop. and Tr. J. 413 (1968). Although there is a significant minority position, a majority of jurisdictions also recognizes a statutory period of redemption in connection with the foreclosure sale. *See generally*, Washburn, *The Judicial and Legislative Response to Price Inadequacy in Mortgage Foreclosure Sales*, 53 S. Cal. L. Rev. 843 (1980). The statutory period, which may extend from two months to ten years, may occur either before or after the sale. *Id.* at 929-932. *See also*, Note, *Statutory Redemption Following Power of Sale Foreclosure in Missouri*, 47 Mo. L. Rev. 309 (1982). As noted above, the statutory period of redemption following the foreclosure of a Minnesota mortgage is generally not subject to extension. Other states recognize a more liberal rule.[5] On the other hand, "in the vast majority of states," including Minnesota, "the mortgagor will have the right to possession during the statutory period, although in one or two states both statutory redemption itself, as well as the right to possession, is conditioned on the posting of a bond by the mortgagor." G. Osborne, *Real Estate Finance Law*, 537 (1979). In addition, as is also noted above, the Minnesota redemption period expires naturally upon the mere passage of time. In other states, however, the purchaser at sale must take further action to complete the foreclosure process.[6]

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[5] In South Dakota, for example, the redemption period may be extended for an additional year if the debtor pays interest, tax, and costs. S.D. COMP. LAWS ANN. § 21-52-13 (1979).

[6] In a number of states, the certificate of sale or sheriff's deed is filed after the sale and after expiration of the period of redemption. *See, e.g.*, Ariz. Rev. Stat. Ann. § 12-1286 (1982); Colo. Rev. Stat. § 38-39-115 (1975 § Cum. Supp. 1980); Nev. Rev. Stat. § 21.220 (1979); Wyo. Stat. § 1-18-104 (1977).

The various state statutes on redemption, in addition to the differences noted above, contain "widely varying phraseology and multitude of details" concerning the parties entitled to exercise the right of redemption and the amounts payable on redemption. *Id.* at 538.

The Bankruptcy Code does not contain a general rule regarding the effect of bankruptcy on state statutory redemption periods. On the other hand, the Bankruptcy Code contains various provisions which give debtors and their trustees limited extensions of time in which to take certain curative action and which prevent creditors from taking certain actions directed against a debtor or his property. Two of these provisions, found in Sections 108 and 362 of the Bankruptcy Code, were considered by the Eighth Circuit in this case. *Johnson*, 719 F.2d at 275-278. The Eighth Circuit found as a matter of statutory construction that Sections 108 and 362 of the Bankruptcy Code provisions cannot be interpreted to permit the Bankruptcy Court to suspend indefinitely the running of the Minnesota statutory period of redemption following foreclosure.[7] The Eighth Circuit, however, made no attempt to establish a general rule to be applied in all situations and in all jurisdictions. The Court recognized, indeed, that the statutory variations noted above may work to bring the redemption statutes of other states within the scope of the Bankruptcy Code. *Id.* at 277.

This case represents a situation in which the operation of the Bankruptcy Code cannot be made the same in all states.

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[7] The Eighth Circuit also indicated, however, that Section 108 of the Bankruptcy Code may operate to grant a debtor or his trustee a limited, sixty day extension of the time in which to redeem property from foreclosure. *Id.* at 278. Section 108, as construed by the Eighth Circuit, represents Congress's reconciliation of the concerns expressed in the Petition with the requirements of state law.

See, Stellwagen v. Clum, 245 U.S. 605, 613 (1918). Clearly, because the "applicable law varies from State to State, the results in federal bankruptcy proceedings will also vary." *Butner*, 440 U.S. at 53. Accordingly, review of the Eighth Circuit's interpretation of the federal bankruptcy law should be withheld until such time as the Court is presented with an issue of more general application.

3. A Review By This Court Is Not Necessary To Resolve A Conflict Between The Circuits.

The Petition argues that the decision of the Eighth Circuit is inconsistent with the opinion reached by the Ninth Circuit eleven years ago in *Hamblen v. Federal Savings and Loan Insurance Corp. (In re Thomas J. Grosso Investment, Inc.)*, 457 F.2d 168 (9th Cir. 1972). The Ninth Circuit's opinion, however, is easily distinguishable from the situation under review.

While the Ninth Circuit indicated, without analysis, that the predecessor to Section 105 of the Bankruptcy Code "would seem to support" an order extending Arizona's statutory period of redemption, the Court also indicated that "the question directly presented, however, is the applicability" of two of the predecessors to the automatic stay provisions of Section 362 of the Code. *Id.* at 171. The Ninth Circuit held that these two specific provisions, when applied to the foreclosure of an Arizona mortgage, authorized the extension of the redemption period beyond the time specified by the Arizona statute.

The Arizona foreclosure statute considered by the Ninth Circuit differs in several major respects from the statute considered in Minnesota. In particular, under Arizona law, the sheriff's certificate is delivered *after* expiration of the

redemption period. *Id.* at 170. By contrast, as previously noted, the foreclosure process in Minnesota is essentially completed upon sale. The Eighth Circuit's opinion in this case suggests in unmistakable terms that such a difference in state procedure may require a different result in Bankruptcy Court. *Johnson*, 719 F.2d at 277.

In addition, the automatic stay provisions considered by the Ninth Circuit specifically provided that the filing of a bankruptcy petition will stay a pending "mortgage foreclosure . . . proceeding." *Id.* at 171, *quoting* 11 U.S.C. § 548 (1976). This reference to mortgage foreclosures is noticeably absent from the current Bankruptcy Code.

Clearly, a conflict among the circuits cannot be inferred from dicta appearing in a pre-Bankruptcy Code case. It is clear, on the contrary, that the issue decided by the Eighth Circuit was, as the Court noted, "a matter of first impression among the circuit courts." *Johnson*, 719 F.2d at 273. For the reasons advanced above, the Eighth Circuit's opinion may have little impact outside of the state of Minnesota. In any event, however, absent additional decisions from the Eighth and other circuits, it will be difficult, at best, to determine the extent to which the opinion under review will influence decisions arising under different statutory systems.

4. The Unique History Of The Issue Decided By The Eighth Circuit Requires That The Court's Opinion Be Upheld As A Proper Application Of Traditional Standards Of Statutory Construction.

The Petition argues that a review by this Court is necessary to resolve general questions concerning the equitable jurisdiction of the Bankruptcy Court to alter state law. The unique statutory and case law history of the federal bankruptcy law,

however, indicates that the Eighth Circuit's opinion may be upheld as a sound application of traditional standards of statutory interpretation. Accordingly, it would be inappropriate under the facts of this case for the Court to consider the general questions suggested by the Petition.

Section 75 of the Bankruptcy Act of 1898, unlike current law, contained language that expressly stayed expiration of state redemption periods in cases involving the reorganization of family farming enterprises:

> In all cases where, at the time of filing the petition, the period of redemption has not or had not expired, . . . the period of redemption shall be extended . . . for the period necessary for the purpose of carrying out the provisions of this section.

11 U.S.C. § 203 (1940) (expired 1949). Section 75 represented an exception to the general rule in other bankruptcy cases that state periods of redemption were *not* subject to court extension as a result as part of a bankruptcy proceeding. *Johnson*, 719 F.2d at 277, *citing*, *Town of Agawam v. Connors*, 159 F.2d 360 (1st Cir. 1947), *cert. denied*, 330 U.S. 845 (1947); *Garber v. Bankers' Mortgage Co.*, 27 F.2d 609 (D. Kan. 1928); *In re Hageman*, 10 F. Supp. 716 (D. Kan. 1935); *In re Klein*, 9 F. Supp. 57 (D. Minn. 1934); *In re Nelson*, 9 F.Supp. 657 (D.S.D. 1935).

The unique statutory and case law history represented by the authorities cited above provides strong evidence of Congress's intent in this area. *Id.* Accordingly, since the Eighth Circuit's opinion may be upheld as a proper application of traditional standards of statutory construction, it is unnecessary in this case to consider the general questions raised in the Petition regarding the equitable jurisdiction of the Bankruptcy Court to alter state-created property interests.

CONCLUSION

The Eighth Circuit's opinion is the first circuit court opinion under the revised Bankruptcy Code to address the question of whether the Bankruptcy Code permits an extension of a state statutory period of redemption following mortgage foreclosure. The Court's opinion, moreover, arose in the context of a specific statutory scheme, and the reasoning advanced by the Eighth Circuit may have little impact on the cases arising in other jurisdictions. Prior case law and statutory history indicate, moreover, that the Eighth Circuit's opinion may be upheld as an example of sound statutory interpretation. It is also clear, finally, that the Eighth Circuit's opinion is in accord with the general principles most recently addressed by this Court in *Butner v. United States*, 440 U.S. 48 (1979).

For the foregoing reasons, the Petition for a Writ of Certiorari should be denied.

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